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FM AMEMBASSY JAKARTA  
TO RUEHC/SECSTATE WASHDC 0008  
RUEATRS/DEPT OF TREASURY WASHDC  
INFO RUEHXS/ASSOCIATION OF SOUTHEAST ASIAN NATIONS  
RUCPDO/DEPT OF COMMERCE WASHINGTON DC  
RUEHKO/AMEMBASSY TOKYO 2464  
RUEHBJ/AMEMBASSY BEIJING 5362  
RUEHBY/AMEMBASSY CANBERRA 3000  
RUEHUL/AMEMBASSY SEOUL 4884  
RUEAIIA/CIA WASHDC

UNCLAS JAKARTA 001694

SIPDIS  
SENSITIVE

DEPT FOR EAP/MTS AND EB/IFD/OMA  
TREASURY FOR IA/MALACHY NUGENT  
COMMERCE FOR 4430/KELLY  
DEPARTMENT PASS FEDERAL RESERVE SAN FRANCISCO FOR CURRAN  
DEPARTMENT PASS EXIM BANK  
SINGAPORE FOR SBAKER  
TOKYO FOR MGREWE  
USDA/FAS/OA YOST, MILLER, JACKSON  
USDA/FAS/OCRA CRIKER, HIGGISTON, RADLER  
USDA/FAS/OGA CHAUDRY, DWYER  
USTR WEISEL, EHLERS

E.O. 12598: N/A

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SUBJECT: BI CONTINUES RATE HIKES DESPITE INFLATION DIP

11. (SBU) Summary. On September 4, Bank Indonesia (BI) increased its overnight reference rate 25 basis points for the fifth consecutive month, despite a dip in inflation in August. While price increases slowed in aggregate, food and education prices continued to climb. Lower world commodity prices eased price pressures but also contributed to a negative trade balance in July, putting downward pressure on the Rupiah. In addition to raising the overnight rate, BI continued to intervene in the foreign exchange market to support the value of the Rupiah. Foreign exchange reserves fell by \$2.2 billion during the month of August. End Summary.

August Inflation Slows, but Food Prices Remain High  
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12. (U) Inflation slowed on a month-on-month basis in August, dropping to 0.51% from 1.37% the previous month, due in large part to a moderation in the price of global commodities, especially oil. The yoy inflation rate now stands at 11.85%. Domestic food and education prices continued to rise in August, accounting for the bulk of the month-on-month price increase. Food prices have increased 20.1% since August 2007. Prices of protein-rich foods such as poultry and eggs continued to soar in August due to high feed costs, bringing their year-to-date increase to 70.7% and 27.0%, respectively. Wholesale prices have increased at a faster pace than consumer prices. According to the most recent published data, the wholesale price index jumped 6.0% month-on-month from May to June, bring the year-on-year wholesale inflation rate in June to 35.0%.

BI Continues to Tighten  
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13. (SBU) BI continued to tighten monetary policy in September and signaled the use of multiple monetary tools, in moves applauded by most analysts. Despite slower price increases in August, BI increased its overnight reference interest rate to 9.25% from 9.0%, citing ongoing inflationary pressures from strong domestic demand. Key concerns include the rapid growth in bank credit (35% year-on-year as of mid-August) and the surge in imports (52.3% year-on-year in June). Analysts also note that wholesale firms have not yet fully passed on price increases to consumers. As in previous months, BI hinted at plans to raise reserve requirements to

slow loan growth in the coming months.

14. (SBU) BI also continues to intervene in the foreign exchange market, using \$2.2 billion in foreign exchange reserves to defend the value of the Rupiah in August alone. Indonesia's foreign exchange reserves currently stand at \$58.4 billion. Indonesia recorded a trade deficit in July due to strong demand for imports and declining world prices for Indonesia's commodity exports. Analysts expect these trends to continue, putting downward pressure on the currency and triggering additional intervention from BI to control imported inflation. Investors are likely to pay close attention to Indonesia's foreign exchange reserve levels and trends as an indicator of balance of payments and macroeconomic stability in the coming months. Indonesia recorded an overall balance of payments surplus of \$1.3 billion in the second quarter of 2008; however, short-term capital inflows were the primary driver of the surplus.

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